

## Message Text

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ACTION EA-14

INFO OCT-01 ISO-00 SP-03 AID-20 EB-11 NSC-07 RSC-01

CIEP-03 TRSE-00 SS-20 STR-08 OMB-01 CEA-02 L-03 H-03

PA-04 PRS-01 USIA-15 CIAE-00 COME-00 FRB-03 INR-11

NSAE-00 XMB-07 OPIC-12 LAB-06 SIL-01 ABF-01 FS-01

DRC-01 EUR-25 /185 W

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P 091030Z AUG 74

FM AMEMBASSY TOKYO

TO SECSTATE WASHDC PRIORITY 3846

C O N F I D E N T I A L SECTION 1 OF 2 TOKYO 10415

PASS TREASURY OPENING OF BUSINESS FOR COOPER AND CROSS

E.O. 11652: GDS

TAGS: EFIN, JA

SUBJECT: RECENT FOREX MARKET AND RELATED DEVELOPMENTS

REF: (A) TOKYO 1099; (B) TOKYO 9914; (C) TOKYO 9062

SUMMARY: SPOT YEN CONTINUED TO WEAKEN, TRADING BELOW 300 LEVEL FOR VIRTUALLY ENTIRE WEEK. ON DAILY AVERAGE BASIS LOW OF 303.10 YEN PER DOLLAR WAS REACHED ON FRIDAY. VOLUME FOR WEEK WAS UNCHANGED AT \$463 MIL SPOT, \$627 MIL FORWARDS, AND \$312 MIL SWAPS. MOST ANALYSTS GENERALLY PESSIMISTIC ABOUT PREVENTING FURTHER YEN SLIDE BECAUSE OF DIFFICULTY IN ATTRACTING SUFFICIENT FOREIGN BANKING FUNDS TO SUCCESSFULLY ROLL OVER MATURING BANK BORROWING ABROAD AND TO FINANCE JAPAN'S CURRENT ACCOUNT AND CAPITAL EXPORT NEEDS. FOLLOWING IS FINATT'S ASSESSMENT OF CURRENT SITUATION BASED ON TALKS WITH FORMER VICE MIN INAMURA (VICE MIN YOSHIDA CURRENTLY ILL) AND KNOWLEDGEABLE LOCAL BANKERS. ADDITIONAL INFORMATION TO BE DEVELOPED NEXT WEEK WILL BE TRANSMITTED

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SEPARATELY ALONG WITH PROVISIONAL JULY B/P FIGURES.

1. BOJ HAS INTERVENED "MODERATELY" TO MAINTAIN ORDERLY FOREX MARKET CONDITIONS. INTERVENTION THIS WEEK AMOUNTED TO \$10 MIL COMPARED WITH DOLLAR SALES OF ABOUT 40 MIL IN PREVIOUS WEEK. INAMURA SAID GOJ OPERATING ONLY UNDER GUIDELINE 1 OR PERHAPS 2 OF RECENTLY ADOPTED GUIDELINES FOR THE MANAGEMENT OF "FLOATING RATES." HE QUICKLY DENIED THAT JAPAN HAD YET SET ANY "TARGET ZONE OF RATES" AND CONSEQUENTLY WAS NOT OPERATING UNDER GUIDELINE 3. HE BELIEVED GOJ WAS PREPARED TO CONTINUE MODERATE INTERVENTION TO DEAL WITH SUDDEN AND TEMPORARY MARKET PRESSURES IF THAT PROVED NECESSARY. CURRENT PSYCHOLOGY OF MARKET WAS STABLE AS YEN IN FORWARD MARKET REMAINS AT SMALL PREMIUM. MOF ALSO PROVIDING JAPANESE BANKS WITH FOREX THROUGH DIRECT DEPOSIT OF DOLLARS.

2. GOJ HAS TAKEN SEVERAL MEASURES TO EASE THE CURRENT SHORTAGE OF FOREX BY: (1) LIBERALIZATING MAXIMUM AMOUNTS PERMISSIBLE FOR ADVANCE RECEIPT OF EXPORT PAYMENTS (SEE REF (?)); (2) INCREASING AMOUNTS UNDER SWAP LINES FROM \$1.5 BIL TO \$2 BIL; AND (3) FURTHER \$40 MIL INCREASES IN AMOUNT OF IMPACT LOANS FOR AUGUST AND SEPTEMBER. WHETHER THESE MEASURES WILL CREATE ADEQUATE FOREX INFLOWS DEPENDS ON MARKET CONDITIONS AND DEVELOPMENTS ABROAD, SAID INAMURA, BUT KNOWLEDGEABLE BANKER FORESEES LITTLE NET INFLOW INTO JAPAN AS RESULT OF THESE MEASURES IN THE WEEKS AHEAD (SEE PARAS 4 AND 5 BELOW).

3. IN REPLY TO QUESTION OF WHY YEN DECLINING IN FACE OF IMPROVED JAPANESE TRADE PERFORMANCE, INAMURA SAID THAT CURRENT ACCOUNT AS A WHOLE IS STILL IN DEFICIT. ADVANCE FIGURES ON CERTIFIED EXPORTS AND EXPORT LETTERS OF CREDIT SUGGEST JULY EXPORT TRADE FIGURES WILL SHOW 60 PERCENT IMPROVEMENT OVER A YEAR AGO. HOWEVER, IN AUGUST EXPORT RECEIPTS LIKELY TO BE DOWN BECAUSE HOLIDAY CLOSURES WILL BE MORE SEVERE THIS RECESSION YEAR. THUS IN AUGUST RECEIPTS OF CURRENT EXPORT SHIPMENTS MAY BE INADEQUATE TO MEET PAYMENTS OF MATURING IMPORT USANCE CREDITS. IN MONTHS AHEAD FURTHER EXPORT IMPROVEMENT WAS POSSIBLE. MOST OF THE EXPORT GAIN REPRESENTS HIGHER EXPORT PRICES THIS YEAR AND VOLUME

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GAINS HAVE BEEN MORE MODEST. IMPORT GROWTH, ON THE OTHER HAND, HAS APPARENTLY CEASED. INAMURA ACKNOWLEDGED THAT CAPITAL EXPORTS HAD ALSO BEEN AN IMPORTANT FACTOR IN CREATING LARGE FOREX DEMANDS BY JAPANESE BANKS AND INCREASES IN OFFICIAL RESERVES HAD BEEN ANOTHER FACTOR (DURING JAN-JUNE BANKS BORROWED NET OF \$8 1/2 BIL IN LIQUID FORM, WHEREAS CURRENT ACCOUNT DEFICIT AMOUNTED TO ONLY \$5.7 BIL). IN REPLY TO FINATT QUESTION, INAMURA SAID

JAPANESE BANKS HAD INVESTED SOME \$1.8 BIL IN ITALIAN GOVERNMENT AGENCY BONDS THIS YEAR AND THAT DIRECT INVESTMENTS OVERSEAS HAD ALSO BEEN LARGER. FINATT ALSO NOTES THAT JAPAN EXIM BANK LOANS HAVE INCREASED AT RATE OF ALMOST \$200 MIL A MONTH THIS YEAR.

4. JAPANESE SOURCES SAY CURRENT FOREX "SHORTAGE" IS DUE TO DIFFICULTIES JAPANESE BANKS AND NON-BANK BORROWERS ARE ENCOUNTERING IN ROLLING OVER LARGE MATURING SHORT-TERM FOREIGN CREDIT. U.S. SOURCES, ON OTHER HAND, SAY THAT MAINTAINING CREDIT LINES TO JAPANESE BORROWERS CREATES NO PROBLEM BUT THAT CAPITAL LIMITATIONS ARE RESTRAINING BANKS FROM INCREASING LOANS TO ALL POTENTIAL BORROWERS. EMERGENCE OF SO-CALLED "JAPAN RATE" IS MERELY A DEVICE BANKERS ARE USING TO DISSUADE ANXIOUS JAPANESE AND OTHER BORROWERS FROM BORROWING ADDITIONAL AMOUNTS UNDER PREVIOUSLY ESTABLISHED LOAN COMMITMENTS. INAMURA SAID MOF HAS PRESSED BANKS VERY HARD TO OBTAIN FUNDS IN EURO OR U.S. MARKETS. MORE RECENTLY MOF HAS LIMITED ABILITY OF BANKS TO PAY MORE THAN 0.5 PERCENT ABOVE GOING RATE.

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INFO OCT-01 ISO-00 SP-03 AID-20 EB-11 NSC-07 RSC-01

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EUR-25 DRC-01 /185 W

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P 091030Z AUG 74

FM AMEMBASSY TOKYO

TO SECSTATE WASHDC PRIORITY 3847

C O N F I D E N T I A L SECTION 2 OF 2 TOKYO 10415

PASS TREASURY OPENING OF BUSINESS FOR COOPER AND CROSS

5. KNOWLEDGEABLE U.S. BANKERS BELIEVE \$500 MIL INCREASE IN SWAP LIMIT WILL NOT BE QUICKLY UTILIZED. FUNDS CAN EARN PERHAPS 13.5 PERCENT IN JAPAN PLUS SWAP PREMIUM OF 2 PERCENT WHICH NOT A VERY BIG INDUCEMENT OVER CURRENT U.S. RATES. MOREOVER, ADDITIONAL SWAP FUNDS CANNOT BE USED TO MAKE LOANS IN JAPAN THEREBY DEVELOPING NEW CUSTOMER RELATIONS, FOR IT WOULD MERELY WEAKEN BOJ TIGHT MONEY POLICY. BOJ IS PERMITTING ADDITIONAL SWAP PROCEEDS TO BE USED ONLY TO REPAY BORROWING OR TO LEND IN (1) CALL MONEY MARKET, (2) BILL DISCOUNT MARKET, OR (3) TO BOJ. UNDER FRB RULES SUCH PLACEMENTS ARE CONSIDERED RISK ASSETS SUBJECT TO OVERALL CAPITAL LIMITATIONS ON BANKS. DURING FIRST WEEK OF INCREASED SWAP LINE, ABOUT \$100 MIL WAS UTILIZED ACCORDING TO BOJ OFFICIAL.

6. JAPANESE LOCAL PRESS HAS ALREADY REPORTED SALE TO ARAB OIL COUNTRY OF Y10 BIL OF JAPA TEL AND TEL PUB CORP. BONDS. INAMURA NONCOMMITAL ABOUT POSSIBLE FURTHER GOJ APPROACHES DIRECTLY TO ARAB OIL COUNTRIES. HOWEVER, INAMURA HAS SUBSTANTIAL PREVIOUS BOND SALES EXPERIENCE IN U.S. PRIOR  
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TO IET IMPOSITION. HE MAY WELL BE DEVELOPING IDEAS ON HOW GOJ CAN TAP PETRO-DOLLARS DIRECTLY. THIS WOULD PROVIDE GREATEST FOREX RELIEF IN PRESENT CIRCUMSTANCES WHEN U.S. BANKING SYSTEM UNABLE TO MEET JAPANESE DOLLAR DEMANDS.

7. ANOTHER WAY OF EASING DOLLAR "SHORTAGE" HAS BEEN THROUGH DIRECT MOF DOLLAR DEPOSITS WITH JAPANESE BANKS. THESE DEPOSITS HAD PREVIOUSLY BEEN WITHDRAWN IN ORDER TO BOLSTER OFFICIAL RESERVES. SOME \$200-300 MIL HAS NOW BEEN REDEPOSITED IN AUGUST. INAMURA WELL AWARE THAT THESE DEPOSITS CAN HAVE EXCHANGE MARKET IMPACT EVEN THOUGH FUNDS ARE NOT PLACED THROUGH FOREX MARKET. EMBASSY UNCERTAIN WHETHER THIS NON-INTERVENTIONIST ROUTE IS COVERED UNDER THE GUIDELINES ON FLOATING.

8. COMMENTS: JULY TRADE AND PAYMENTS FIGURES AVAILABLE NEXT WEEK WILL INDICATE EXTENT TO WHICH JAPAN'S BASIC BALANCE HAS STRENGTHENED OR WEAKENED. HOWEVER, EMBASSY CONSIDERS PRESENT SITUATION ONE OF GREATLY OVEREXTENDED AND ILLIQUID JAPANESE BANKING SYSTEM WITH RESPECT TO ITS FOREIGN CURRENCY ASSETS AND LIABILITIES. JAPANESE HAD ALWAYS EXPECTED U.S. BANKING SYSTEM TO BE "LENDER OF LAST RESORT" BUT MISJUDGED THE EXTENT OF THOSE LIMITS. UNDER GOJ PRESSURE, BANKS ARE DESPERATE TO ROLL OVER EXISTING SHORT-TERM INDEBTEDNESS BECAUSE ASSETS CANNOT BE RUN OFF AS LONG AS CURRENT ACCOUNT AND LONG-TERM CAPITAL BALANCE IS

IN DEFICIT, COUNTRY'S FOREX NEEDS MUST BE SUPPLIED IF  
NOT BY THE BANKING SYSTEM THEN BY RESERVES OR ELSE  
PRESSURE WILL HAVE TO BE PLACED ON RATE. IMPACT OF RECENT  
RATE DECLINE HAS BEEN SEVERE ON DOMESTIC OIL COMPANIES  
WHOSE YEN PRICES ARE STILL FROZEN. HOWEVER, JAPANESE ARE  
BEGINNING TO RECOGNIZE THAT EXPORTERS STAND TO BENEFIT  
ESPECIALLY AT A TIME WHEN DOMESTIC DEMAND IS LIKELY TO REMAIN  
SLACK FOR MANY MONTHS. EMBASSY NOT YET IN A POSITION TO JUDGE  
WHETHER GOJ USED ILLIQUID POSITION OF BANKING SYSTEM AS  
RATIONALE FOR RECENT DECLINE IN YEN RATE.  
HODGSON

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## Message Attributes

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